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Argentina: Challenges Facing the Alfonsin Administration

Special National Intelligence Estimate
Memorandum to Holders

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The Director of Central Intelligence
Washington, D.C. 20505

National Intelligence Council

3 December 1984

MEMORANDUM FOR: Recipients of Memorandum to Holders of
Special National Intelligence Estimate 91-2-83:
CHALLENGES FACING THE ALFONSIN ADMINISTRATION

SUBJECT: Argentina's Credit Position

1. Since the NFIB approval of captioned estimate on
27 November 1984, there has been a significant new development
in Argentina's relations with its creditors. [redacted]

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2. A loan arrangement reached between Argentina and its bank
advisory committee and other creditors on 2 December 1984 reduces
much of the short-term uncertainty regarding Argentina's financial
situation. [redacted]

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[redacted] Since adequate trade credit lines
seem assured, Argentina's ability to obtain needed imports during
early 1985 is no longer a question mark. However, the ability of
the Alfonsin government to maintain sufficient compliance with its
IMF program to allow continued drawings of its IMF and bank loans in
1985 remains uncertain. [redacted]

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MEMORANDUM TO HOLDERS

SNIE 91-2-83

**ARGENTINA: CHALLENGES FACING
THE ALFONSIN ADMINISTRATION**

Information available as of 27 November 1984 was used in the preparation of this Memorandum to Holders, which was approved by the National Foreign Intelligence Board on that date.

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THIS ESTIMATE IS ISSUED BY THE DIRECTOR OF CENTRAL
INTELLIGENCE.

THE NATIONAL FOREIGN INTELLIGENCE BOARD CONCURS.

The following intelligence organizations participated in the preparation of the Estimate:

The Central Intelligence Agency, the Defense Intelligence Agency, the National Security Agency, and the intelligence organizations of the Departments of State and the Treasury.

Also Participating:

The Assistant Chief of Staff for Intelligence, Department of the Army

The Director of Naval Intelligence, Department of the Navy

The Assistant Chief of Staff, Intelligence, Department of the Air Force

The Director of Intelligence, Headquarters, Marine Corps

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SCOPE NOTE

President Alfonsin was elected to a six-year term by a large margin in October 1983. His initial prospects were examined in December 1983 in SNIE 91-2-83, *Argentina: Challenges Facing the Alfonsin Administration*. This Memorandum to Holders updates that Estimate and assesses the political and economic outlook for his government over the next year or so. It focuses on President Alfonsin's performance and prospects on these critical issues:

- The need to stabilize the domestic economy and come to terms with international creditors.
- The dismantling of the armed forces' political power base and the potentially catalytic effects this has on antigovernment elements in the military.
- Relations between the government and its political opponents, especially the Peronists.
- The course of Argentine foreign policy, including relations with the United States. [redacted]

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KEY JUDGMENTS

While Argentine President Alfonsin faces some near-term risk in pursuing his political and economic objectives, we believe he will remain in office for at least the next year or so. Institutional disarray among his opponents—the armed forces and the Peronists—and his energy and personal dynamism are his strongest assets. Moreover, his unflagging advocacy of democratic government has helped him to identify his own survival with the survival of Argentine democracy, which we believe has largely insulated him from the negative effects of his mounting difficulties. We believe, however, that, to do more than simply survive in office, Alfonsin will have to build on these strengths, exert more decisive leadership, and overcome administrative difficulties that have stymied the formulation of coherent policies. [redacted]

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We believe that Alfonsin's economic performance will largely determine whether he ends his next year in office in a strengthened or weakened position. Thus far, he has often subordinated economic necessities to his political objectives, arguing that an economic austerity program would pose a threat to Argentina's nascent democracy. While this posture helped to bolster his position in the early days of the administration, accelerating inflation eroded some of his popularity and projected an image of a government adrift. [redacted]

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Even though Buenos Aires signed an accord with the International Monetary Fund (IMF) in September and has taken steps to curb wage and price increases and monetary growth, we believe that an acceptable level of compliance with Fund terms is unlikely beyond early 1985. This is primarily because Alfonsin is reluctant to take harsh economic measures that he believes may promote recessionary trends and popular resistance. We also foresee difficult negotiations with commercial lenders for debt rescheduling even after formal approval of the accord is obtained. We judge that even a delay in formal approval—scheduled for December—is possible, which would further impede domestic recovery in 1985 by limiting the growth of necessary imports. Without new money—and banks so far have balked at providing the major share of the \$5.5 billion Buenos Aires contends it needs through the end of 1985—it is likely that Argentina will face temporary cash flow shortfalls, selective production bottlenecks, and further interest arrearages. [redacted]

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On balance, we believe the odds are slightly greater than even that the current IMF program will unravel before much of the money—either from the Fund or the banks—is disbursed. In that event, we ex-

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pect that Alfonsin, the IMF, the banks, and the industrialized governments would try to renegotiate the agreement sometime next year. Under such circumstances, Argentina is likely to continue to "muddle along from crisis to crisis" for the next year or so. [redacted]

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If Alfonsin continues to temporize in economic policy and, consequently, Argentina falls out of compliance with its IMF program, new credits may become unavailable. This may result in a moratorium on interest payments and eventually a declaration of default by creditors. Nevertheless, we believe that such a breakdown with creditors is unlikely. Both the Argentines and the banks very much want to avoid such a crisis. Alfonsin would not want to take on the long-term risks entailed in a financial break with the West. Furthermore, foreign banks apparently have little leverage on Argentina because of its favorable foreign trade position, and thus they would seek to avoid a permanent rift with Buenos Aires. [redacted]

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Concerning the internal political situation, we expect Alfonsin's relations with the military to remain strained, but we foresee little likelihood of any serious armed forces challenge to his administration during the next year. Alfonsin has tried to maintain a balanced approach in dealing with the military, moving forward with structural changes and budget cuts while working to limit human rights investigations and consulting the high command on sensitive issues. Most officers still believe Alfonsin's administration is dominated by leftists, but they seem resigned to civilian rule and are trying to cope with the changes. Moreover, while we cannot rule out more organized opposition, and perhaps a local garrison uprising, dissidents remain scattered and lack a figure around whom to rally. In our view, only a dramatic departure from administration policy, especially on the human rights issue, would galvanize antigovernment sentiments enough for the armed forces to reassert themselves. [redacted]

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We also see little likelihood that the main opposition party, the Peronists, will reach any meaningful agreement with the government, despite Alfonsin's continued efforts to negotiate a political-economic accord. They appear intent on exploiting Alfonsin's indecisiveness, political miscalculations, and poor economic performance to help unite their fractured party, and they have used their plurality in the Senate to stall or force compromises on key legislation. The Peronists will probably continue a dialogue and may at least temporarily acquiesce in a mild austerity program. Nevertheless, we foresee continued labor strife and increasingly intense antigovernment rhetoric as union bosses face internal elections and politicians gear up for congressional elections beginning early next year. [redacted]

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Alfonsin has adopted a pragmatic foreign policy intended to refurbish Argentina's international image. To this end he has searched, thus far with limited success, for initiatives that will enhance his image in both the West and the Third World. For example, he has tried to promote regional solidarity, democratic government, superpower disarmament, and debtor relief. He has reached an agreement with Chile on the Beagle Channel dispute and undertaken new initiatives to bring the United Kingdom to the negotiating table to reduce tensions over the Falkland Islands.

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Alfonsin has maintained the good relations with Moscow and Havana begun by the military after the Falklands war.

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The Argentines have shied away from projects that would allow a large, permanent Soviet presence

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Alfonsin has sought a close relationship with Washington, and we expect him to continue efforts to strengthen ties, play down differences, and emphasize areas of common concern. As a result, we believe the Argentines will be sensitive to rebuffs of their initiatives, as well as to efforts to press them on nuclear policy differences. Bilateral relations, however, will be most vulnerable to tensions introduced by Argentina's economic difficulties. The Alfonsin government expects US help in resolving its financial problems as proof of Washington's support for democracy.

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A collapse of debt negotiations would be likely to prompt intense Argentine efforts to win regional support for a confrontation with the banks—though with little chance of success, in our view—and Alfonsin would probably use the United States as a scapegoat. In a worst case, Alfonsin could be tempted to retaliate against US commercial and financial interests in Argentina. Moreover, the subsequent financial crisis would probably lead to new opportunities for Cuba and the Soviet Union to ingratiate themselves in Buenos Aires with offers of political support.

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DISCUSSION

The First Weeks—A Quick Start

1. President Raul Alfonsin moved swiftly to implement campaign promises in the weeks following his December 1983 inauguration, both to demonstrate his leadership and to exploit the momentum of his victory and the disarray among his Peronist and military opponents. To bring to Argentina what the President called the "rule of law," for example, he forcibly retired several dozen members of the military high command, restructured the hierarchy to subordinate clearly the services to civilian rule, and initiated investigations into human rights violations committed by security officials during the antiterrorist campaign of the late 1970s. Politically, he took steps to institutionalize his electoral coalition and to build bridges to the defeated Peronists, calling for a national unity government and offering them posts in his administration. On the economic front, Alfonsin implemented measures he hoped would break the inflationary cycle and made initial contacts with domestic business groups and foreign creditors. At the same time, he moved to end Argentina's diplomatic isolation, pledging support for regional democratic forces and seeking a major role in the Contadora peace process in Central America.

2. In our view, however, Alfonsin's strategy, while generating popular enthusiasm for his administration and keeping his opponents off balance, fostered unrealistic expectations within both his coterie and the electoral coalition. [] his backers expected a quick turnaround in the economy, without an austerity program; resolution of the foreign debt problem; full investigations into human rights abuses; and rapid moves to break the power of the Peronist unions and the military. In our judgment, by encouraging inflated expectations so early in his tenure, Alfonsin left himself little maneuvering room to alter his policies and increased his vulnerability to criticism from his opponents.

Administration Character and Style

3. Alfonsin has stayed close to the Radical Civic Union Party's moderately left-of-center populist platform, and we believe virtually all his policies and most of the rhetoric have been driven by his overriding goal

of defending democratic government. Alfonsin continues to behave as though he is still running for office as he endlessly stumps the country calling for national unity and warning of the dangers of political particularism. At the same time, he has dedicated considerable energy to further broadening his party's political base, including efforts to win over the traditionally Peronist working class. Key to his plans to build this following []

[] has been his effort to institutionalize his electoral majority—including Radical and Peronist elements—into what he has called the "third national movement." []

4. Alfonsin's economic policy has also been shaped by long and deeply held moderately left-of-center Radical populist tenets. On the domestic side, the President is morally and politically committed to economic growth and real wage increases, especially for those on the low end of the salary scale. Moreover, most of his economic proposals have been aimed at modestly redistributing income to the lower classes. On the foreign debt issue, Alfonsin shares the Radical belief that the current high rates of interest on loans and commission fees to bankers are usurious.

5. Alfonsin's political and economic views have struck a responsive chord with the electorate—recent polls show he commands broad popular backing—but, in our view, his single-minded focus on protecting democratic government has also proved a liability. While we had earlier estimated that Alfonsin would effectively use his electoral mandate and the considerable powers of the presidency to follow up on his initiatives, [] he has frequently chosen to back off and search for compromise when his measures have met resistance. This has been especially true, for example, in dealing with the Peronist-dominated labor unions. Moreover,

[] putting the protection of democracy above all other objectives has encouraged Alfonsin to avoid making tough decisions, especially on economic policy, that might alienate elements of his constituency. At the same time, [] the President's refusal to move decisively has reinforced the image of

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an administration adrift by exacerbating traditional splits within his own Radical Party. [redacted]

Challenged by the Economy

The Domestic Scene

7. We believe that Alfonsin, largely because of political and social concerns, has failed to develop any consistent domestic stabilization program. He has resisted implementing what he sees as potentially destabilizing policies, such as large spending cuts and tough wage restraints. Moreover, [redacted]

[redacted] he lacks the staff support necessary to develop a realistic budget, and he has faced bureaucratic resistance to requests for detailed spending and investment plans from bloated public-sector agencies. As a result, his administration has developed little more than a patchwork of inconsistent policies aimed

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at balancing competing interests. Further, while willing to tackle the military budget, Alfonsin has tried to head off labor unrest through large wage increases that violated the government's original inflation fighting plan. [redacted]

8. These patchwork economic policies have produced some domestic recovery, but at the cost of driving inflation higher. The Argentine Central Bank reported a 3.3-percent gain in economic activity in the first quarter, as real wage increases sparked an industrial recuperation and strong foreign demand and favorable weather led to another dynamic agricultural performance. [redacted] unemployment has eased, while heightened spending on social welfare programs, according to the press, has also contributed to improved living standards. Inflation, however, has accelerated to over 600 percent in recent months. Higher taxes, real wage increases, daily devaluations, import controls, and the government's failure to restore fiscal and monetary discipline have combined to fuel an upward spiral. Although Argentines have demonstrated the ability to cope with higher living costs by resorting to moonlighting, the underground economy, and financial speculation, inflation is exacting a toll. According to press [redacted] reports, capital flight continues, spot shortages of goods have emerged, and private investment is depressed. Moreover, the Peronists have begun to make inflation a domestic political issue. [redacted]

The External Sector

9. An improved foreign trade position has been the greatest economic bright spot, but the surplus is still not large enough to meet the interest payments on the debt. Booming agricultural exports and tough import controls have resulted in a \$3.5 billion trade surplus for the first nine months of 1984, according to the press. The administration has used increased foreign exchange earnings to rebuild reserves to about \$1 billion, to settle past-due trade payments, and, lastly, to make enough interest payments to try to avoid a downgrading by US regulators of loans to Buenos Aires. In early November, however, the regulators did downgrade private debt to the substandard level.¹ These policies have now left the Alfonsin government unable to reduce an estimated \$2 billion in overdue interest payments, inherited from the military. Moreover, Alfonsin has been unable to move forward in rescheduling some \$20 billion in debts and arranging

¹ "Substandard," according to the Department of the Treasury, referred in this case to loans on which the interest was more than 90 days overdue.

new lending to close a projected current account gap. [redacted]

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loans. We expect there will be problems in the debt talks unless governments or international financial institutions provide a large chunk of the \$5.5 billion needed. Moreover, we are not confident that Argentina will be politically able to maintain acceptable compliance with the terms of an IMF accord beyond March 1985. [redacted]

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Current State of Play

12. Alfonsin is currently engaged in selling the IMF accord to the Argentine electorate. [redacted]

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Troubled Relations With Key Political Actors

13. On the basis of Alfonsin's tough campaign rhetoric, the strength of his electoral win, and the disarray among traditional Argentine power brokers—the military and the Peronists—we estimated that he would move swiftly and decisively to curb the power of the services and the Peronist-dominated unions. His goal was to prevent a resurgence of historical ties between military officers and the Peronists, groups he holds responsible for Argentina's chronic economic and political instability. Alfonsin has been less aggressive in this regard than we estimated before, however, because of difficulties in forming a coherent administration, political miscalculations, and a hesitancy to alienate key interest groups. The narrow defeat of his critical labor reform bill in March was a further setback.

Civil-Military Relations

14. We judge that Alfonsin has had some success in bringing the military under civilian control by taking a balanced approach on key issues, although relations remain strained. In general,

[redacted] he recognizes that the services are too weak to resist strong reforms, but he also understands the military's long-term threat to civilian rule and has tried hard to avoid the appearance of routinely interfering in military affairs. For example, the President forced several dozen members of the military high command into retirement, but left the lower ranks alone and allowed the services to determine how to implement budget cuts and changes in the command structure. On the human rights front—the most sensitive area in civil-military relations—Alfonsin has sought to control the scope of the investigations and trials, as well as public criticism of the armed forces. At the same time, he and his Defense Minister maintain a steady schedule of garrison visits to hear grievances and bolster morale.

15. Alfonsin's efforts have done little to assuage military concerns, however, and most officers, while acquiescing in civilian government, oppose most government policies. Armed forces grievances include:

- Insufficient pay compared to the private sector.
- Severe budget cuts that have forced cutbacks in conscription and training and threaten vital military-owned industries.
- Human rights investigations that could go beyond the senior ranks.

— The government's intention to reorient the military away from its internal security role and involvement in national politics.

— Their perception of the general leftist tone of the administration and the influence of those they regard as leftists.

Preoccupation with these issues and discontent at all levels have increased steadily since mid-March. Financial stringencies and uncertainty have profoundly affected morale, induced thousands of badly needed noncommissioned officers to leave the military, and deflected attention away from the task of rebuilding the services.

[redacted] Public manifestations by rightwing military dissidents have also occurred in recent weeks.

16. We also believe that the disarray and budget cutbacks in the services are adversely affecting military capabilities and readiness. For example,

[redacted] flying time for combat pilots has been reduced, naval maneuvers have been cut back, and reductions in conscription have hampered all three services. Moreover, in order to reduce operating expenses and raise funds, the Navy has been forced to consider selling several modern ships and submarines, which military planners view as key in rebuilding the post-Falklands Navy.

[redacted] the government has shaved funding for ongoing military research and development efforts and for investment in military-owned industries. The press reports that the administration has, however, decided to allow continued military control of key defense plants and, indeed, the administration is supporting efforts to increase weapons exports as a way of moving these facilities toward self-sufficiency.

Alfonsin and the Peronists

17. The Peronists apparently have not evolved into the loyal opposition movement that many Peronist and Radical leaders, including Alfonsin, envisioned in the weeks following the election. Most Peronist political and labor leaders have ignored the President's initial calls for bipartisan government and sought to exploit Alfonsin's vacillating policies and poor economic performance. As a result, rather than folding under the weight of deep and longstanding Peronist disunity and administration pressures, the Party has used its plurality in the Senate and the threat of strikes to win concessions on union reform and other key proposals,

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The Military Under Alfonsin

President Alfonsin has made considerable efforts to curb the military's political power. At the same time, he remains committed to the creation of a strong national defense establishment.

Alfonsin has altered the military high-command structure in order to subordinate the services more clearly to civilian authority. In addition, he has undertaken a restructuring of forces, sharply cut back operational funds, and initiated a reorientation of military doctrine to deemphasize its internal security role and stress defense against external aggression. His long-term goal is to transform the armed services into a democratically oriented, highly professional military force capable of countering outside threats to Argentine sovereignty.

For their part, service commanders, despite the political and economic pressures wrought by the transition to civilian government, have in varying degrees begun to implement lessons learned from Argentina's defeat in the Falklands conflict in 1982. Leaders of Argentina's Navy, which numbers about 36,000 personnel, shocked by the British sinking of the Argentine cruiser Belgrano and also troubled by the Navy's inability to counter the British "exclusion zone" around the Falklands, have worked the hardest to address deficiencies. The addition over the next several years of eight previously ordered ships and two modern submarines—if not sold—will greatly enhance Argentina's deepwater capability. The delivery since the war of the last nine of 14 Exocet-capable French Super Etendard aircraft previously purchased from France will further bolster the Navy's ability to challenge hostile ships.

Argentina will soon have the best equipped Navy in South America. Nevertheless, manpower and financial constraints may limit its effectiveness.

such as nuclear policy. Moreover, the constant work stoppages, sometimes affecting millions of workers, have forced the government to make wage and other economic concessions that have further complicated economic stabilization plans.

18. We believe that Alfonsin's wavering on tough policy decisions has cost him his postelection psychological edge and forced him into a conciliatory, if not defensive, posture. This has been especially apparent since mid-March, when his labor reform bill was defeated and efforts to cut inflation began to flag. He granted large wage increases to public-sector workers

Commanders of the 18,000-man Air Force have continued, [redacted] to upgrade the capabilities of aircraft already in their inventories

Although the performance of the 85,000-man Army in the Falklands war was the worst of the three services, Army commanders thus far have taken only limited steps to address shortcomings.

We expect the Argentines, despite sharp financial constraints, to pursue their cost-efficient reequipment program.

At the same time, Argentina's difficulties in obtaining materiel during the Falklands war and in its aftermath have reinforced the military's determination to produce essential equipment domestically. Senior officers are hoping to expand the country's already-considerable arms-manufacturing capabilities and to move forward with existing and new coproduction agreements with foreign firms—primarily in Western Europe. President Alfonsin, concerned about military backlash against his civilian regime, has supported these efforts. He has also backed away from his earlier plans to turn military industries over to the private sector. Finally, he has supported an intensified arms export drive, which he sees as a key way of providing additional sources of revenue for the military as well as acquiring needed foreign exchange for his government.

and concluded a short-lived political accord with the Peronists. New discussions—ambitiously aimed at forging a social pact with labor and business on economic issues—began in July, but have made little headway. The Peronists, themselves deeply concerned about inflation and potentially increasing unemployment, may acquiesce in a mild austerity program, but any long-term support for government economic policies is unlikely in our view.

19. Peronist politicians are preparing for the 1985 congressional elections—occurring in some provinces as early as next March—and they probably will have

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to temper their antigovernment rhetoric to avoid potential voter backlash. Earlier this year, one Peronist admitted that the movement had actually lost popularity since last December, underscoring its alienation from the electorate and the difficulty inherent in challenging Alfonsin's popularity. Moreover, recently conducted polls of union and nonunion workers showed little sentiment for the use of strikes to win concessions. Furthermore, the partial failure of a general strike in September, which surprised some union leaders, clearly demonstrated their lack of appeal.

- In Central America, he continues to view strengthened ties with Nicaragua as a key to promoting regional peace, but he has become disillusioned with the Sandinistas' domestic policies, and he has moved toward a more balanced posture in the region.
- Domestic opposition has slowed his efforts to reopen negotiations with the United Kingdom on the Falklands, although he is likely to continue his endeavors.

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Meeting Foreign Policy Objectives

Limited Gains

20. Alfonsin has adopted a pragmatic foreign policy, and his goal has been to make Argentina and himself key actors on the international stage. To this end he has sought to:

- Break what he believed was Argentina's diplomatic isolation following seven years of military rule and the Falklands war.
- Promote Latin American solidarity, human rights, and democratic government in neighboring countries.
- End Argentina's military presence in Central America and assume a role in the Contadora peace process.
- Reach an accord with the Chileans on the Beagle Channel dispute and reduce tensions with the United Kingdom over the Falkland Islands.

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21. By moving on so many fronts, Alfonsin was probably searching for an initiative that would enhance his political stature at home and abroad, but results have been mixed. For example:

- His leadership of the Cartagena Latin American debtors group has probably heightened his prestige in the Third World, but has hurt him in the West.
- In the Southern Cone, Alfonsin has backed away from openly supporting democratic opposition groups, fearing that such support would damage bilateral relations and provide the military in those countries with an excuse to slow their own transitions to civilian rule.

Improving Relations With the United States

22. In relations with Washington, we believe Alfonsin has sustained his initial efforts to strengthen ties, avoid confrontations, and gain a close relationship.

The administration has also publicly emphasized Argentina's traditional ties to the West.

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Further, at times when Washington would have been a useful target for Alfonsin, especially on the debt issue, he has exercised restraint and

would not allow the debt issue to interfere in bilateral relations.

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23. Nevertheless, we believe potentially serious bilateral irritants remain. Most important is the perception of the Argentine public that the United States can influence the IMF and private bankers and can control interest rates. Thus far, Alfonsin has avoided this tack, and he responded positively to Washington's assistance in arranging the interest payment rescue packages in March and June. The President, however, initially tried to internationalize the debt issue in order to pressure the IMF and private lenders to show more flexibility on loan criteria. The Argentines have also sought to institutionalize their dialogue with the United States in an informal high-level hemispheric study group, and they expect a positive response from Washington. Buenos Aires's decision to deemphasize Central America as a contentious point with Washington could be quickly reversed by any indication of an expanded US military role. The Argentines have also deliberately played down differences over nuclear pol-

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icy, but persistent US pressure, especially as Argentina seeks to export its nuclear technology, could also increase tensions.

The Soviet Union and Cuba

24. Alfonsin has maintained good relations with Moscow and Havana. This trend was begun by the military government after the Falklands war in 1982 to protect its grain market—Argentina sold over 40 percent of its 1983 grain exports to Moscow—and to demonstrate independence from the United States. Buenos Aires has had difficulty identifying Soviet finished goods it could import to redress a growing trade imbalance, but it has signed some contracts—most initiated before the election—for Soviet participation in hydroelectric and port modernization projects.

Buenos Aires has also signed a new trade agreement with Havana, which significantly increased the credits available for Cuban purchases over the next several years.

25. While the Soviets and the Cubans have reaped commercial gains, in our view they have been unable to parlay their relationship into greater political influence in Buenos Aires.

sustain public support for civilian government and have prevented the early coalescing of traditionally antidemocratic forces. Moreover, while he has fallen short of popular, as well as his own, expectations, Alfonsin has taken important steps to redress the worst abuses of his military predecessors and to subordinate the services to civilian authority. At the same time, his determination to continue a dialogue with the opposition, to move toward an IMF agreement, and to maintain a tough stance against military dissidents suggest that he is becoming sensitive to the limitations of his electoral mandate. We believe he has demonstrated willingness to accommodate domestic interest groups and political rivals as well as to assert his presidential authority on occasion.

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27. We believe that, unless he more consistently exercises presidential authority, however, he will have major difficulties in overcoming the still-serious economic problems Argentina faces. While his determination to subordinate economic policy imperatives to political objectives has helped to build a prodemocratic consensus and contain his opposition, it has hindered implementation of sound measures and generated the impression of a government adrift. Overcoming this image will require Alfonsin to use more consistently the powers of his office to contain divisions within his administration and to overcome opponents in Congress, the Peronist party, and the military. It may also require a dramatic change in his closed leadership style. Alfonsin's hesitancy to delegate authority and inclination to focus on details have distracted him from major issues, and his reliance on a small coterie of advisers has shielded him from alternative views. Moreover, we believe that he must make steady progress in reorienting Argentine political institutions toward accepting compromise rather than deferring to the military for solutions to pressing national problems.

28. Despite these formidable political and economic challenges, we expect Alfonsin to remain in office for at least the period of this Estimate. He has generated considerable support for democratic government, which many Argentines now believe is tied to his survival. The perception that his removal would mean a return to the chaos and repression of the 1970s helps account for Alfonsin's ability to insulate himself from the negative effects of his mounting difficulties.

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Outlook

Tough Choices for Alfonsin

26. In our view, Alfonsin has made considerable gains during his first 10 months in office. We believe the uncertainties and problems of his administration primarily reflect his inexperience and the immaturity of civilian political institutions. His charisma, constant campaigning, and search for consensus have helped

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Economic Uncertainty

29. In our view, whether Alfonsin ends his next year in office in a strengthened or weakened position will depend primarily on his economic performance.

the President and his close advisers understand the domestic and international implications of failing to stabilize the economy. We believe that Alfonsin will try to implement an adjustment program under IMF auspices.

Maintaining compliance with a Fund accord will be difficult, particularly when it becomes necessary to enact budget, taxation, and other austerity measures.

30. Meanwhile, high inflation is likely to continue despite the IMF agreement, discouraging new investment and eroding purchasing power. Since over the years the Argentines have become psychologically adjusted to living with triple-digit inflation, it is difficult to estimate the public's threshold for enduring high rates of inflation over an extended period. At a minimum, we believe inflation will continue to take a toll on Alfonsin's popularity and may limit his maneuvering room on a range of noneconomic issues. Further, labor and the media would probably begin to question the purpose of continuing economic sacrifices, and members of his own party probably would urge Alfonsin to abandon the IMF track to preserve social peace and avoid election year losses. His supporters would also probably argue that squandering his limited political capital on the debt issue would prevent him from gaining congressional agreement to his military reforms and foreign policy. Military restiveness would also be likely to increase as deteriorating economic conditions intensified social unrest and degraded operational readiness and morale.

31. Even with a Fund agreement, we anticipate slow and uneven progress in debt talks with foreign banks and little likelihood of rescheduling some \$20 billion in loans before yearend. Argentina will probably demand concessions similar to those granted recently to Mexico and Venezuela, delaying a settlement. In the meantime, Argentina will struggle to keep its payments on trade credits current in order to maintain access to such financing.

33. We believe that if bank negotiations for new money begin to drag this will undercut prospects for the economic recovery now under way. Without new loans the country may experience temporary cash flow difficulties. Further, we expect continued problems in obtaining trade financing for imports and attracting foreign investment, both necessary for industrial reactivation and increased employment. As a result, we anticipate that the Argentines will face selective production bottlenecks and will again resort to temporary suspension of payments to ease financial strains.

34. The period through December 1984 will be particularly difficult for Alfonsin because Argentina will have to adhere to IMF conditionality without receiving any funding until the program is formally approved. Moreover, creditor banks will have to promise enough money to fund the program before the IMF board of directors will pass on it. Further delays in negotiations with private lenders could hold up initial disbursals of IMF funds until early 1985.

35. We believe that the odds are slightly greater than even that the current program will unravel before much of the money—either from the Fund or the banks—is disbursed. We believe that Alfonsin wants the program to be successful, but pressure from labor unions may convince him to relent on wage constraints, a move that would jeopardize budget deficit targets. Still, we do not believe that Alfonsin would scuttle the Fund accord—repudiation would remain the last of his options—and he would probably seek a renegotiation of the agreement sometime next year. Indeed, many banks also probably expect Alfonsin to ask for new terms. As long as he continues to show his intentions to stabilize the economy, both the Fund and the lenders—who recognize that Argentina's strong trade position gives it some chance of repudiating its debt and surviving the financial community's reprisals—are unlikely to abandon him. Thus, while

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debt talks probably will suffer temporary halts and setbacks, we see only a 20-percent chance that they would collapse altogether. [redacted]

36. Despite good intentions on both sides, however, we still see at least a slight chance that Argentina will fall so far out of compliance that new foreign credits would be withheld well into 1985. If this occurs, Alfonsin would probably cease servicing interest payments, thus entering into a de facto moratorium. Since this would reflect his failure to control the economy, we would expect inflation to increase even further, followed by severe import restrictions to preserve foreign exchange. Subsequently, labor unrest would escalate sharply as workers pressed for higher wages to keep pace with rising costs. [redacted]

Strained Civil-Military Relations

37. We expect disgruntlement within the military to persist, and probably increase, in coming months. Tensions probably will grow as human rights investigations and budget cuts proceed and general public antipathy toward the military continues to erode morale and discipline. This discontent may stir more organized opposition, and perhaps a local garrison uprising, especially in outlying areas. In our view, the likelihood of more widespread and concerted resistance will be mitigated, however, by:

- The lack of civilian support, a prerequisite for coups in the past.
- The continued [redacted] support of senior commanders for civilian government and their determination to professionalize the services and implement lessons learned from the Falklands defeat.
- Undiminished rivalries between the services and within the Army that would be likely to preclude a united front against the government.
- The lack of a leader around whom lower ranking dissidents could rally.
- Alfonsin's sensitivity to military concerns and his demonstrated willingness to make accommodations when possible and to remove officers who challenge his policies. [redacted]

38. We believe that only a radical shift in Alfonsin's current posture toward the military—especially on the human rights issue—could galvanize antigovernment sentiments and move the services to attempt to reassert themselves within the next 12 months. Nevertheless, deeper budget cuts that threatened military capabili-

ties, the appearance of caving in on pending territorial disputes, or social unrest sparked by deteriorating economic conditions would also dramatically heighten armed forces concerns. [redacted]

Continued Peronist Intransigence

39. We believe that the Peronists will continue to exploit Alfonsin's vulnerability on economic and other issues, which, along with internal Peronist party dynamics, will continue to block any meaningful political accord. The Peronists will almost certainly persist in opposing wage restraint, other austerity measures, and debt negotiations. They are also likely to continue their public criticism of Alfonsin's other policies. [redacted]

[redacted] We expect opposition from both labor and political leaders to intensify as various congressional election dates approach in coming months. [redacted]

40. In our view, however, the Peronists face considerable risks in maintaining their intransigence. The party remains deeply divided and fragmented, held together only by constant opposition to the government, and is losing popularity. Thus, we believe Peronist union bosses will be forced to reevaluate their strategy of staging strikes to force government concessions. For his part, Alfonsin has been quick to turn the Peronists' poor showing to his political advantage, publicly accusing them of irresponsibility. Some Argentine and US observers have suggested that Peronist failures will diminish Alfonsin's drive to accommodate them. We believe that, at the Peronist convention scheduled for later this year, party leaders must achieve significant progress in purging extremists and evolving into a responsible opposition or risk further fracturing in the movement. [redacted]

Frayed Radical Coalition

41. We also expect Radical divisions to worsen as political and economic pressures continue to mount and party extremists challenge administration positions. On the left, Alfonsin will continue to face pressure from Radical youths—who have done considerable damage to efforts to reach an accord with the Peronists—and from human rights advocates demanding more extensive investigations. The right wing will continue to dispute the growing influence of the left within the party, any of Alfonsin's initiatives in Central America, and the ideological adjustments implicit in Alfonsin's efforts to usurp the Peronists' political base. We believe the President will continue to try to balance the views from both camps, but he will ignore for as long as possible entreaties from party leaders to

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call a party convention to elect a new leadership for fear of bringing differences to a head. In our view, internal rifts will continue to hamper the administration's ability to govern, and they could adversely affect Radical efforts to exploit Peronist divisions in the coming elections. [redacted]

Implications for the United States

42. We expect the trend of positive US-Argentine relations to continue, principally because Alfonsin sees Washington's good will as vital in overcoming his economic difficulties and bolstering democratic government in Argentina. Opportunities for cooperation will be greatest on international political issues. For example, we expect Alfonsin to downplay differences over Central America so long as the Contadora peace initiative remains alive and, to continue, at some political risk, to project a more balanced policy in the region. The President's desire to resolve territorial disputes with Chile and the United Kingdom also coincides with US interests, and we believe he will continue to reject renewed military harassment of the British garrison on the Falklands. His decision not to bolster opposition groups in neighboring countries openly should also help US efforts to promote democratic government in the Southern Cone. [redacted]

43. On security issues involving the USSR and Cuba, Washington's interests and those of the Radicals will also coincide, but we see little likelihood that Buenos Aires will back away from commercial ties with Moscow or Havana. Alfonsin will continue to search for alternative markets for grain sales, but the Soviets probably will remain the major buyers for some time. Alfonsin will continue, therefore, to provide Moscow with commercial opportunities to redress the trade imbalance, including construction projects, which will considerably diminish prospects for US sales. We expect, however, that the Argentines will also continue to resist an arms relationship with Moscow. We foresee no change in Alfonsin's view that trade with Havana is useful in demonstrating independence from the United States and in discouraging the Cubans from backing renewed terrorist activity in Argentina. [redacted]

44. Alfonsin's overriding goal of consolidating democratic government in Argentina poses both problems and opportunities for bilateral relations. His constant campaigning and search for consensus has deflected his attention from what many US bankers and officials see as more pressing economic problems. His failure to develop coherent economic policies, combined with his human rights policy and military reforms, has

considerably heightened concerns within the armed forces. Thus, Alfonsin will seek Washington's continuing open support for his democratic government to help keep would-be conspirators in check. He would also probably welcome US military training slots for his officers and increased service-to-service relations, if it would help professionalize the services and steer them away from antigovernment activities. [redacted]

45. Bilateral relations are probably most vulnerable to tensions introduced by Argentina's economic difficulties. We believe that Buenos Aires expects Washington to help bolster Argentine democracy primarily by taking extraordinary steps to help resolve its financial problems. Moreover, Alfonsin, the Argentine public, and many in the Argentine Congress continue to believe that Washington has the power to elicit cooperation from the IMF and US commercial banks and to dictate interest rates. This makes the United States an easy scapegoat for Alfonsin if negotiations with creditors collapse, particularly if the breakdown was in response to large hikes in the US prime lending rate or to austerity "imposed" by the IMF and the banks. [redacted]

46. The Argentines are likely to call, although probably unsuccessfully, on other Latin American debtors through the Cartagena group to act in concert against lenders in the event of a breakdown on debt negotiations. If the situation worsened—particularly if banks or industrialized countries threatened sanctions—Alfonsin might be tempted or forced by internal political pressures to retaliate against US interests. For example, he may block remittance of profits of US subsidiaries or freeze US assets in Argentina. In the unlikely event of a debt repudiation, Washington would have little leverage to bring Buenos Aires back to the bargaining table, and it would open new opportunities for the Soviet Union, Eastern Europe, and Cuba to ingratiate themselves as they proffered political—but no economic—support to help the Argentines weather the confrontation. [redacted]

47. Beyond economics, other potential flashpoints exist. Alfonsin will probably pursue the idea of a formal hemispheric forum proposed earlier this year, and indications that the United States may be unwilling to participate in or support Buenos Aires's initiative would bruise Argentine sensitivities. In addition, while the President is trying to bring the nuclear program under close civilian control, he remains alert to outside pressure over Argentina's reluctance to accept full-scope international safeguards. Buenos Aires also expects continuing support in the United Nations on the Falklands issue. Argentina's efforts to export weapons to sensitive areas, such as the Middle

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A Worst Case Scenario—Debt Moratorium

We believe there is still some chance that, even with an IMF agreement, the Argentines will not maintain compliance with Fund terms and debt talks with foreign banks will collapse.

Real or perceived pressure from the industrialized countries, the Fund, or lenders; a sharp, unexpected rise in prime interest rates; or domestic political pressures, especially from labor, could all scuttle compliance with an IMF adjustment program. Such a breakdown—probably accompanied by a temporary moratorium—would entail major dangers, in our judgment.

We judge that he would also become more assertive in trying to coordinate joint action by Latin American debtors, further increasing tensions with bankers. These developments probably would cause banks to resist new lending at a time when Argentina's cash strains would be mounting.

We believe that, at this juncture, the likelihood that Buenos Aires would halt payments of its debt would increase, although Alfonsin would carefully gauge the domestic and international implications before making such a move. The Argentines might first publicly threaten such an action in an effort to convince banks to extend new credit needed to cover interest payments. If the banks held firm and retaliated by declaring Argentina in default, Alfonsin might calculate—similar to the

military's decision to invade the Falklands in April 1982—that he could appeal to Argentine nationalism to support the government's decision to confront foreign interests.

Buenos Aires would have adequate cash reserves to purchase critical imports, and bankers would be hard pressed to organize a supplier embargo effective enough to seriously disrupt the economy. In addition, because 80 percent of Argentina's exports are agricultural products and half the manufactured exports go to LDCs, they are largely invulnerable to boycott. Moreover, depending on the circumstances, Argentina would probably be able to count on the support of many Third World countries, as well as the Soviet Union, for moral, if not financial, support.

Our projections show that the Argentine economy could weather even a 50-percent reduction in imports and continue to function. The greater danger is that an inflationary psychology would emerge that would force political changes. After an initial period of cooperation induced by nationalistic fervor, Alfonsin's rivals would probably soon distance themselves from the administration, and social unrest would probably increase. Officers would also become increasingly concerned about intensifying civil disorders. As a result, Alfonsin's hold on office could become more tenuous over time.

East, could become a contentious issue. Further, a US decision to expand its military presence in Central America would almost certainly provoke a sharp response.

Indicators of Projected Outcome

48. The following are signs we believe would confirm our analysis that Alfonsin is likely to remain in office over the period of this Estimate, but with only moderate success in resolving Argentina's economic problems:

- Talks with Peronists continue, but do not achieve sufficient progress to curb opposition activity.
- Strike activity persists at about current levels, with sporadic calls for large-scale stoppages.
- Military unrest continues at low levels, with some efforts to organize a united front against Alfonsin and with the potential for limited open hostility toward the government.
- Despite the IMF accord, negotiations with private lenders are slow and the administration has difficulty implementing tougher policies.

- Rifts persist in the Radical Party with increasing prospects for some losses in upcoming elections.
- Overall popularity of government slips, but Alfonsin shows demonstrably stronger leadership and manages to sustain strong support for democratic government.

Alternative Indicators

49. The following are developments we would expect to see if Alfonsin's position were to erode more significantly than we project:

- Negotiations with Peronists collapse, and they consistently block legislation on a range of key issues.
- Strike activity increases, with growing support for general strikes aimed at undermining the government.
- Alfonsin becomes increasingly indecisive and vacillates on responding to unrest.
- Alfonsin clearly backs away from austerity measures, jeopardizing IMF and lending agreements.

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- Inflation stays well above an annual rate of 1,000 percent for three months in a row and appears likely to accelerate.
- Significant rightwing and leftwing terrorism reemerges.

- Military discontent increases and coalesces across service lines.
- Contacts between military and civilian groups increase.
- Active coup plotting begins. [redacted]

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